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# **Organization for Better Accounting and Financial Service**

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*Presented before the Financial Section of the American Drug  
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Members of the Financial Section of American Drug Manufacturers Association:

I am pleased to be with you today to discuss "Organization for Better Accounting and Financial Service", a subject which has been of great interest to me for many years.

We are in a changing world — there is no doubt about it. Scientific developments of the past two decades or so have had a great impact on our civilization.

It is becoming evident that the great developments in the field of nuclear energy will have an effect on all of us. Today we are all most conscious of the atom and hydrogen bombs and realize that the storehouse of these bombs at the present time, in their various sizes and kinds, could obliterate civilization in the event of an all-out war. On the pleasant side, we appear to be on the threshold of the utilization of atomic energy for industrial power and other peacetime uses. We are told that as a result of this development it may be possible to construct plants in sections of the country where heretofore it was uneconomical to do so because of the lack of power, thus bringing more activity and prosperity to communities in diverse areas of the nation.

Expenditures for research by industry have been great and the indication is that they will be progressively greater in the foreseeable future —

New and modern research and engineering centers have been erected to provide every facility to stimulate research accomplishment.

Fellowships have been awarded by industry to educational institutions and individuals to provide for study and research in technological fields.

New and better products have been developed.

Process development has brought about costs which, if it were not for this research, would be much greater.

Let us contemplate for a moment the development of what are termed the "wonder drugs". You know even better than I that illnesses are being cured today quickly whereas before the advent of penicillin, for example, recovery was often drawn-out over long periods of time. By reason of these new drugs and advances in medical science, the life-expectancy of individuals is longer, a matter which has a bearing on current thinking with respect to retirement age of individuals.

Research and, of course, war and threat of war have brought about a tremendous expansion of this country's industrial facilities. This in turn has made it necessary to realign industrial organization so that the larger industrial units may be efficiently managed.

This brings me to the observation that accounting and financial departments must be arranged and, where necessary, improved upon so that they can continue to meet their responsibilities under these changing conditions. Many companies have reorganized their accounting and financial departments to meet these changed conditions, but, on the other hand, there is still much to be done in this area.

It seems manifest that, as corporate and other forms of business organization cannot today remain static, neither can accountants and financial executives fail to recognize the impact of changing conditions.

To anyone genuinely interested in accomplishing a "Better Accounting and Financial Service" to management, I would recommend searching inquiry into four general areas. They are, in progressive order, (1) the accounting organization, (2) the accounting system, (3) the promptness with which accounting and financial data are assembled and given to the management (this is a particular pet of mine, which I have dubbed "The Early Closing"), and (4) the form, content, and calibre of reports to management.

I should like to submit, for your consideration, that the real focal point here is "The Early Closing". Streamlined accounting organization, modern accounting systems, and dynamic reports will not serve their maximum purpose unless the facts are available to management early.

Few companies today accomplish the monthly closing of accounts in a quiet and orderly manner. Most managements are anxious to know the results of operations as soon in the following month as is practicable of attainment, and in many cases sooner. Certainly, early financial information places management in an advantageous position.

I can recall, in my experience, that about twenty-five years ago

management generally was satisfied and pleased to have the previous month's figures by about the 25th to the 30th of the current month. Through the years, however, the gap between the end of the month and the deadline for closing of accounts, and rendition of financial reports, has narrowed. As a matter of fact, there is pressure on the accounting and financial group in many companies today, particularly in the larger ones, to close the accounts and complete financial reports at an early date in the month — for example, the eighth of the month. Such an early closing is attainable. In my own experience, a closing as early as the fourth of the month has been accomplished and, I might add, with reliable results.

#### Early Closing Not Based Upon Estimates

It might be well to mention at this point that my conception of an early monthly closing presumes accuracy, and is based upon a complete month's operations. I am aware that some companies close their accounts early in the month by reason of an early cut-off of the previous month. Such a practice does not coincide with my thinking.

I recommend to the accounting and financial officers here today, if you have not already accomplished an early closing of your company's accounts, and by an early closing I mean certainly not later than the fifth of the month, that you give this objective primary consideration. The first report rendered to management under such an early closing plan might be called a "Condensed Financial Report" which would set forth the sales and net income of each operating division, and each subsidiary company, for the month and year to date. It might also show comparisons with the budget and with the same factors for the previous year. Detailed financial reports can follow a little later.

#### A Good Accounting Organization is Necessary

To accomplish "Better Accounting and Financial Service", first, the form of accounting organization should be considered and selected in the light of the circumstances peculiar to the business.

Many corporations today are organized by operating divisions based largely upon the type of product manufactured, and staff departments, of which the accounting and treasury departments are examples, which serve the company as a whole.

In some companies the accounting function is centralized in the executive offices. In such cases the accounting personnel in divisional offices are engaged only in gathering information to be forwarded to the central point.

In other companies the accounting function is completely decentralized, each operating division having its own accounting department responsible for preparation and rendition of complete financial and cost information to the division. Here, the accounting group in the executive offices concerns itself mainly with the consideration and interpretation of the divisional information for purposes of the consolidated financial reports.

There are differences among companies as to whom the accounting department personnel reports. In some corporations all accounting personnel report to the chief accounting or financial officer, while in other companies the operating division management is given responsibility for such personnel. In practically every case, however, the accounting policies are set by the principal financial officer in collaboration with the top-management.

Based upon my experience, it is preferable to have all accounting personnel of a company report to the chief accounting or financial officer rather than to others who have not been trained to direct and guide the accounting functions. Uniform procedures are easier to accomplish and maintain if all accounting work is under one central authority; better accounting and financial service and an early monthly closing are easier of attainment.

On the question of centralization or decentralization of accounting records — in my opinion it is desirable to centralize financial accounting, while on the other hand it is preferable to have the cost accounting performed in divisional or plant offices. The gathering, recording, and presenting of data relating to cost of production should be done at the point of manufacture, where it can be used most effectively. However, with increasing use of all-purpose giant computers, it seems to me that there will be a trend toward centralization of plant accounting records also.

It seems unnecessary to say that accounting personnel should be carefully selected. In addition to proper training in accounting, English, finance, and economics, attention should be given to personal appearance and ability to work with others.

#### Good and Modern Accounting System Needed

The next item to consider in "Organization for Better Accounting and Financial Service" is a good modern accounting system. This is needed both for a company which manufactures only one product as well as for a company manufacturing a multiplicity of products, and for a

single-location unit as well as for a multiplant operation. While my remarks today are aimed at companies whose business is concerned with the manufacture of several products, they do have application also to the small company.

I believe you will agree that a company which must wait for the computation of actual costs for the month for the costing of its sales can hardly expect to close promptly. On the other hand, if an up-to-date standard cost system is used, the costing of sales can be accomplished more readily, which is an important factor in accomplishing a better accounting service. This brings me to an expression of opinion that an early closing cannot be accomplished without the use of standard costs or some other system of predetermined costs.

The plan of accounting for sales should produce sales figures on either the first or not later than the second day of the month. Expeditious reporting of shipments must be made to the invoicing point or points throughout the month and of course copies of invoices should reach the accounting department as quickly as possible thereafter. If several invoicing points are used the last day's or two-days' billings should be transmitted from the outlying points to the accounting department by telegraphic or other means of rapid communication. The matter of communication between points, as we know, is being improved daily. The rapid accumulation of monthly sales figures is mandatory to prompt accounting service; it can be attained today through proper organization, assisted by modern methods of communication, such as transceivers.

The prompt receipt of purchase invoices is equally important. The lack of attention today to rapid invoicing by such a large segment of business is probably a continuing surprise to all of us. Invoices from vendors should arrive at about the time of receipt of the goods or services. In most cases you will find it necessary to make a special request of many vendors to render their invoices more promptly. Of course, the internal organization must be so arranged that invoices are processed promptly. The recording of the receipt of goods, purchasing-department procedures, and accounting for purchases, all require careful attention in the design of a modern accounting system.

With the current expansion of business many companies have had to construct new plant. I mention this for the reason that the accounting for construction requires advance planning if complete and accurate information is to be accumulated. This problem can be resolved by

close cooperation between the accounting and engineering departments. I know from personal experience that problems arising from construction, which at times may be of considerable concern, can be solved.

Inventories are another major problem in any accounting system. If sales are considered through the end of the month, it naturally follows that figures on month-end inventories must be obtained, and the inventory figures should be available immediately after the end of the month.

Many companies take physical inventories, particularly of finished and in-process product, each month. Often, difficulties arise if these inventories are taken on the last day of the month. It has been my experience that in some cases it is practicable to make physical counts a day or so before month-end, and by applying subsequent movements, obtain dependable figures.

Other inventories such as raw materials and supplies are in most cases recorded on a perpetual basis so that no problem as to inventory-taking is experienced. The usages of raw materials and supplies should, however, be reported punctually by the plant or plants.

With this audience it is not necessary to go into detail on each item entering into a good accounting system. I might just state that everyone in an organization charged with the responsibility for furnishing basic accounting data, such as the plant-payroll section and the like, must be organized so that the required information can be gathered expeditiously and sent through proper channels to the accounting department, in compliance with a predetermined time schedule.

I should like to make one more point before discussing briefly modern accounting machines. As much should be done prior to the close of each accounting period as is practicable. Entries affecting depreciation, prepayments, accruals, and other items can be completed beforehand and need not be delayed.

#### Modern Accounting Machines Can Be of Assistance in Early Closing

Through the development of electronic data-processing machines a new and valuable tool has been fashioned to aid business in the complex problems of administration and research. These machines have wide potentialities.

The original giant electronic computers were devised solely for use in solving complex mathematical problems in connection with United States Government research in various fields concerned with defense preparations.

Now we have electronic computers designed particularly for accounting. I was in a position to watch the development of one of these computers and to supervise its application to accounting work. These machines, by reason of their high-rental or purchase price, will find use only in companies of considerable size.

There are, however, other electronic machines which will find a place in smaller companies. I have had the experience also of using one of the smaller electronic computers in many accounting applications, and although this machine cannot accomplish as much as the later-designed, large, all-purpose computers, it is nevertheless a very effective machine.

Almost every phase of accounting work can be done on the all-purpose electronic data-processing computers, including the preparation of the financial statements. I have seen accounting reports which previously took 200 man-days a month in preparation completed by the use of the electronic computer in 20 hours.

I know you have all read and heard other persons speak about these machines in great detail and therefore I shall not do so. I shall say just this —

1. It is better to use the punched-card machines to a considerable extent in your accounting before adopting the electronic data-processing machines. It may be possible to make the transition to the EDP machines by circumventing the punched-card systems, but it seems a very difficult way to proceed.
2. Learn all you can about electronic data processing before adapting your procedures to any such equipment. It is usually desirable to assign a group to study very carefully for a period of time the workings and usages of such equipment.
3. After the machines have been placed in use you will find many problems which must be solved, and patience will have to be exercised.

In my opinion, we shall soon have certain companies performing all accounting record-keeping on electronic data-processing equipment. This will occur in companies which are progressive also in all other phases of management.

It seems to me that the new electronic machines are not only a boon to improved accounting record-keeping but also to accountants personally. The accountant of the future will be more of an interpreter-of-facts than a recorder-of-information.



## Reports to Management

The value of a good accounting and financial organization and of an early closing is lessened unless good standards of reporting to management are employed. Because of the magnitude of this subject of reporting to management I shall treat it this morning only in a broad and general way.

I have mentioned earlier the "condensed report" which might be rendered early, which alerts the management quickly to the financial results for the period.

After this report is rendered, the accounting and financial department should concern itself immediately with the preparation of a complete financial report for each operating division. Such report might include:

1. A balance sheet with comparative figures for the previous month and as of the end of the previous fiscal year.
2. A statement of income for the month and year-to-date with budget comparison.
3. A supporting schedule to the statement of net income by plants and important segments of each division.
4. Condensed statements of selling, administrative research, and other expenses compared with the budget, and
5. Detailed statements of sales, by each product, containing budget comparison.

Such financial reports are more valuable if they contain comments of the accounting or financial officer highlighting the more important happenings of the period. These comments may relate to the comparison of the actual figures with the budgeted amounts and comparisons of actual production costs with cost standards and other facts. Interpretation of figures is a valuable function of the accounting and financial department.

It is my opinion that the report to the Directors should be designed to furnish information about the financial affairs of the company in a concise and easily understandable manner. Accordingly the balance sheet and income statement included in this report might be in briefer form than in the other financial reports. The statement of income, nevertheless, should contain budget comparisons and other information which the Board considers necessary to a proper appraisal of the effectiveness of the active management.

One of the most important statements of a Directors' Report should be a statement of estimated cash requirements for a specified period. In determining estimated cash figures, there must be taken into consideration projected earnings, depreciation and other provisions not requiring cash outlay, and anticipated construction expenditures. A statement of cash requirements forms a basis for determining when additional capital is needed. Obviously, without such information, it would be very difficult for the management of a company to foresee cash requirements and to determine when additional capital is needed.

With your permission I shall draw upon my experience in describing some of the principles which I consider important in designing and presenting reports to management for greater financial service.

First, the appearance of a report is most significant. Information which is presented on a printed form in a manner facilitating easy reading receives far more attention than a hand-written or a completely typed report. The use of different colors for the printing and ruling is very effective in financial statements.

Second, the information shown on a report should be pertinent. It is desirable to discuss with the management group which is to receive the report the type of information planned. In a company which has several plants it is usually very desirable to have reports covering the operations of each plant contain similar information. Such uniformity of reports permits comparison between plants. Exceptions may be made, however, if the reason for the deviation is sound. For instance, a general manager of one of the divisions may have a little budget scheme of his own and may request that such budget figures be shown, in addition to the regular data in the cost statements for his division. It may be wise to accommodate this general manager. The information he desires is evidently of value to him and, accordingly, of value to the company. This is an example of the difference in the methods of operation between individuals which should be recognized; reports should be prepared accordingly.

Third (I would like to emphasize by repetition), the promptness with which reports are submitted is most important. Information received by executives long after the period covered by the report loses its usefulness as a means of control.

Fourth, the frequency with which reports are issued is significant. Some reports can be furnished bi-monthly or quarterly without loss of effectiveness during times of normal or maximum operation.

In times of economic stress, however, it may be necessary to issue these reports more frequently.

Fifth, it is essential to review all reports from time to time with the executive group to determine whether or not they are serving the purpose for which they are intended. It is often found that during the course of time, the need for information changes and a portion of a report or even a complete report loses its effectiveness and, therefore, can be discontinued. This review should most certainly be made in the event of a change in management.

Sixth, the necessity for accuracy of information in reports cannot be overemphasized. The detection of errors by readers of reports tends to discredit the information submitted, with the result that confidence in figures is lessened. An error in a report might be used to divert attention from the real cause of an unsatisfactory operation with the result that the unsatisfactory condition is not corrected.

Finally, reports should present information in a clear, concise, colorful, and interesting manner. A report which cannot be readily understood loses its effectiveness. To some executives, figures may mean little, and in these cases it may be desirable to present the essential information in the form of charts or graphs. Charts are sometimes a more-effective means of bringing out certain facts than an ordinary report.

#### Cooperation of Management is Necessary

In closing, it might be appropriate to observe that it is difficult for the accounting department of any company to effect organization or systems improvements without the cooperation of management and the company as a whole. It is only human nature for persons to express objection if changes in routine or procedure are made for a purpose which seems somewhat remote from what they are doing.

However, if management will explain their reasons for wanting figures and facts about operations earlier in the month, their other basic reasons for changes, how the individual as well as the company stands to benefit, and how all groups have been requested to cooperate with the accounting department, a great hurdle in accomplishing better accounting and financial service will be overcome.